



## Memorandum 16 /2005

Commonwealth of Massachusetts | Public Employee Retirement Administration Commission  
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Joseph E. Connarton, *Executive Director*

### MEMORANDUM

TO: All Retirement Boards

FROM: Joseph E. Connarton, Executive Director

RE: Update on Private Letter Ruling Request on Pre-Tax Buybacks

DATE: April 28, 2005

In September 2001, the Commission submitted a private letter ruling request to the Internal Revenue Service that, if approved, would allow deductions from salary to purchase creditable service to be made on a pre-tax basis. The IRS had previously issued private letter rulings to the Teachers' Retirement System and to the Boston Retirement System, but these rulings apply only to those Systems. The process for obtaining the ruling for the remaining retirement systems has continued since that time and the ruling has not yet been issued.

As a result, except for members of the Teachers' and Boston Retirement Systems, deductions from salary to purchase creditable service other than the mandatory contributions will continue to be post-tax. Mandatory contributions to the retirement system that are deducted from salary continue to be pre-tax consistent with the IRS private letter ruling issued in 1988. Certain rollovers to purchase creditable service also can be made on a pre-tax basis (see PERAC Memorandum #13/2002).

Enclosed is a copy of a letter from PERAC's tax counsel, Ice Miller, that more fully discusses the status of the private letter ruling request.

If you have questions, please contact PERAC's General Counsel, Barbara Phillips, at (617) 666-4446, ext. 902.

Enclosure



April 14, 2005

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VIA FACSIMILE AND U.S. MAIL

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**Re: Private Letter Ruling Request**

Dear Barbara:

We are writing in response to your letter of March 14 in which you asked us to explain the status of the pending private letter ruling request (now for Worcester Regional Retirement Board). This request was originally submitted on September 12, 2001. We understand that there must be frustration on the part of your retirement systems on this issue, and we hope that this letter can help explain to them the general issues involved and the current status of the request. We must admit we are also frustrated at this point with the delays in reaching a conclusion on this request.

Unfortunately, the area of service purchase pick-ups is one in which the IRS' position has evolved considerably since it initially began issuing rulings on this issue. These earlier rulings (of which there are a number) essentially allowed a governmental defined benefit plan to permit employees to make contributions to purchase service credit (really a voluntary contribution) on a pre-tax basis if such contributions were made pursuant to binding, irrevocable payroll deduction. The basic theory was that the use of an irrevocable payroll deduction took away enough employee control over the contributions (as the employee could not change his mind and instead receive the contributions directly as cash), that the contributions could be treated like employer contributions, and thus made on a pre-tax basis. These earlier rulings did not place specific limits on the number of irrevocable payroll deductions an employee could make, but each deduction had to be irrevocable by its terms.

We received a number of these rulings on our clients' behalf, and although the time frames sometimes seemed longer than necessary, there was a certain predictability on turnaround time. Unfortunately, the situation has changed over the last 18 months in two ways. First, the IRS began to issue service purchase pick-up rulings which were much more restrictive, often including the following limitation language:

This ruling is based on the conditions that (1) a participant who elects to purchase a particular type of service credit may not make more than one irrevocable election to purchase that type of service

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credit; and (2) a participant may make more than one irrevocable election to purchase service credit provided any subsequent election is for the purchase of a different type of service credit, is irrevocable, and does not alter or amend the terms and conditions of any prior election to purchase service credit.

PLR 200410025 (March 3, 2004); PLR 200347020 (November 7, 2003).

During the negotiation on the currently pending ruling request, the IRS requested similar limiting language, to which we agreed.

Second, the timing has become more and more erratic and delayed. For example, the IRS agent working on this request advised us on several occasions since November of 2003 that the IRS was generally holding all ruling requests on service purchase pick-ups pending internal policy meetings to decide the appropriate rules for these service purchases. Our experience has been that generally this is the case, except for some very simple, mandatory contribution pick-ups, which are still being processed to completion. We have a number of clients who are caught in this same backlog.

In a conference call this week, the IRS agent reported that a draft ruling will be sent in the next week to the IRS Chief Counsel Office to seek their agreement with the position that the potential for multiple irrevocable payroll deductions is permissible, so long as there is only one irrevocable election for a particular type of service. She said that it is difficult to provide us a timetable for when a decision could be expected from the Chief Counsel Office, but that it would be at least a month. Nonetheless, we are encouraged that at least this case is moving again.

We too wish this matter was concluded so your systems could install the programs they and their members want to have. We will continue to monitor this ruling. We hope that this information is helpful to you. Please let us know if you have any additional questions.

Very truly yours,

ICE MILLER

A handwritten signature in cursive script that reads "Mary Beth Braitman (LEH)".

Mary Beth Braitman

A handwritten signature in cursive script that reads "Lisa Erb Harrison".

Lisa Erb Harrison

MBB/LEH:pjb

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